



STORKEY & Co
MANAGEMENT CONSULTANTS

Management of Portfolio of Financial Assets

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Let me cover ...

What defines a
portfolio of
financial assets

Examples of
financial asset
portfolios

The case of
New Zealand

IPSAS 15 Definition

A financial asset is:

- Cash
- A contractual right to receive cash or another financial asset from another entity
- A contractual right to exchange financial instruments with another entity under conditions that are potentially favorable
- An equity instrument of another entity

IPSAS 15 Financial Instruments

- Financial instruments include both primary instruments, such as receivables, payables and equity securities, and derivative instruments, such as financial options, futures and forwards, interest rate swaps and currency swaps
- Derivative financial instruments, whether recognized or unrecognized, meet the definition of a financial instrument and, accordingly, are subject to IPSAS Standard
- **For DMOs, it covers cash, securities and derivatives that are maintained for meeting debt obligations and hedging risks**
- Financial asset portfolio should be valued at the amount for which each asset could be exchanged between knowledgeable, willing parties in an arm's length transaction, i.e. fair value, which will be the “market” price for traded instruments or “derived” price for non-traded instruments

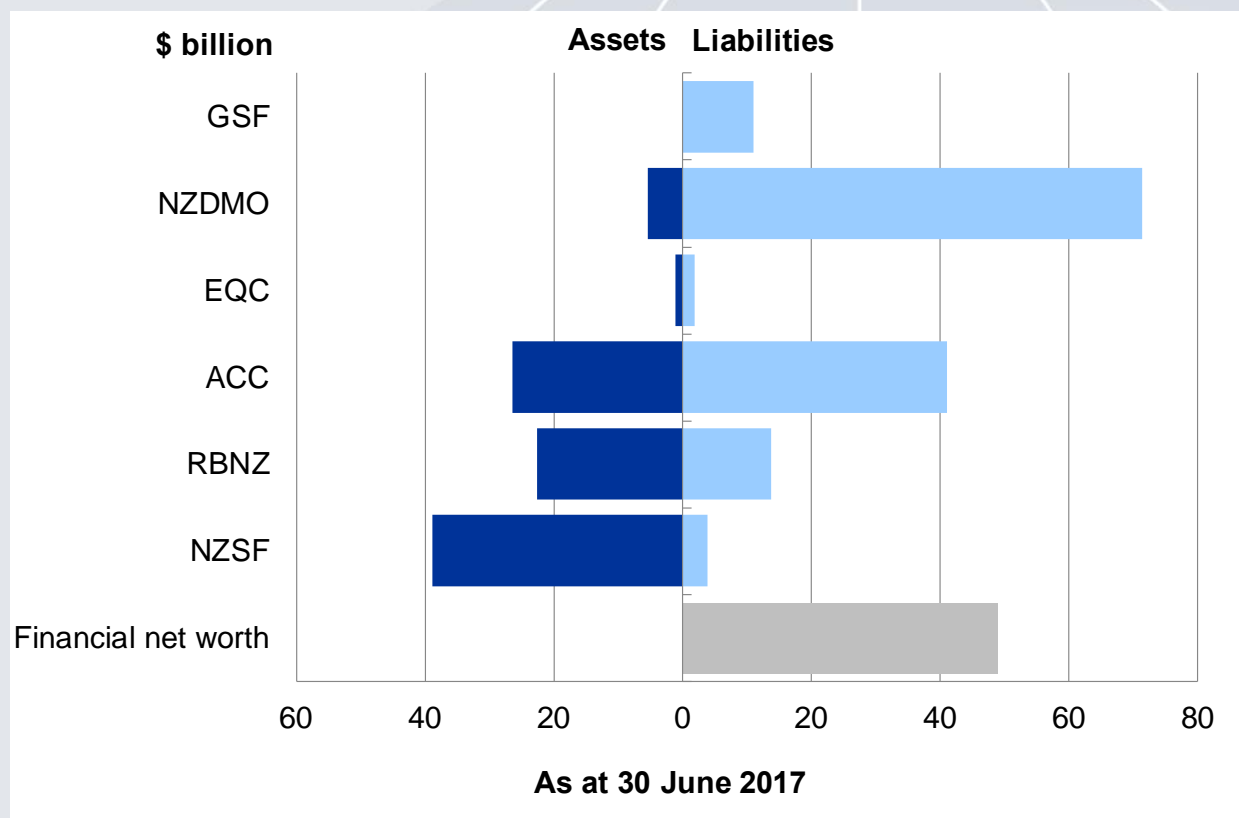
Example of Financial Asset Portfolios

1. Foreign exchange reserves
 - managed by the central bank (may involve fund managers)
2. Cash and liquidity portfolio
 - managed by DMO or Treasury (cash management)
3. Financial investment portfolio (including derivatives)
 - managed by DMO but could be placed with central bank particularly for foreign currencies
4. Sovereign wealth fund (~ 44 countries)
 - managed under own legislation or by fund managers
5. Other designated funds
 - disaster risk such as SEADRIF, insurance & pension funds, student loans, sinking funds, guarantee redemption fund

Financial Balance Sheet of New Zealand

- “Notional” NZDMO balance sheet can be “completed” by including other Crown financial assets
- Objective is to manage wider Crown balance sheet risk
- On this basis, a “big five” list of financial assets are included in NZDMO’s ALM framework (GSF, EQC, ACC, RBNZ, and NZSF)

Figure 21 – Financial balance sheet



Source: The Treasury

Financial Asset Portfolios in NZ

Financial assets

	Note	Actual	
		30 June 2017 \$m	30 June 2016 \$m
<i>By class</i>			
Cash and cash equivalents		18,732	15,617
Reinsurance, trade and other receivables	12	4,905	4,342
Long-term deposits	13	4,730	4,791
Derivatives in gain	13	4,381	5,888
Marketable securities	13	39,558	40,822
IMF financial assets	13	1,837	1,897
Share investments	14	30,700	24,217
Kiwibank loans	15	17,795	16,689
Student loans	15	9,197	8,982
Other advances	15	1,591	2,563
Total financial assets		133,426	125,808

Source: NZ CFS as at 30 June 2017

NZDMO Derivative Portfolio

	Notional Value As at 30 June 2017		
	Derivatives in gain \$m	Derivatives in loss \$m	Total Notional value \$m
Foreign exchange	64,964	14,803	79,767
Cross currency swaps	11,122	5,469	16,591
Interest rate swaps	42,183	55,027	97,210
Futures	2,037	3,371	5,408
Other derivatives	20,400	13,077	33,477
Total derivatives	140,706	91,747	232,453

Source: NZ CFS as at 30 June 2017

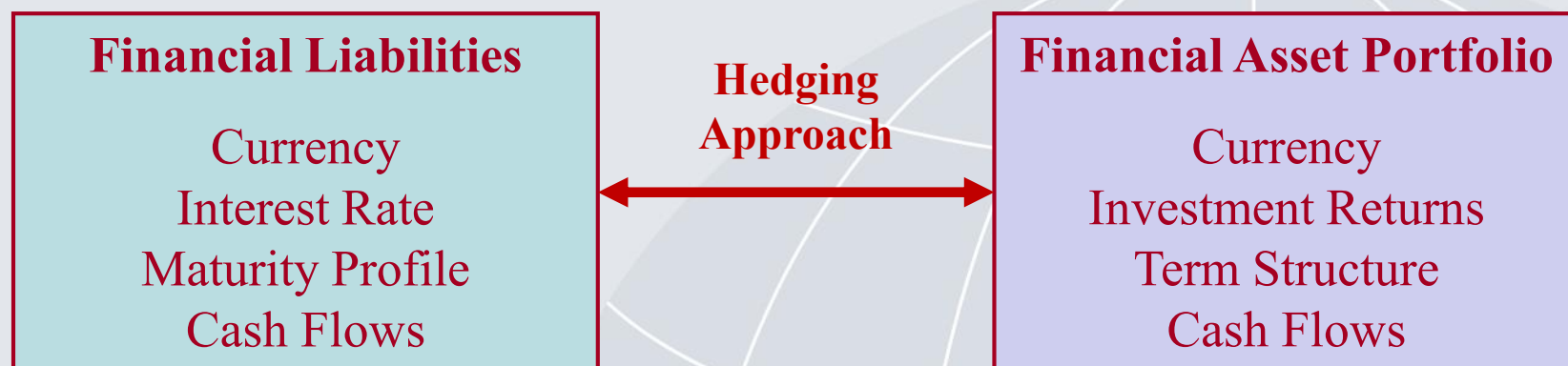
NZDMO Asset Portfolio

- NZDMO managed asset portfolios that, at 30 June 2017, included marketable securities of NZ\$7.1 billion and a cash balance of NZ\$7.8 billion
 - invested in AAA and AA rated securities
- Liquidity risk is managed on an individual entity basis generally by maintaining adequate reserves, banking facilities and reserve borrowing facilities, by continuously monitoring forecast and actual cash flows
- The Government expects to meet its obligations from operating cash flows, from the results of bond tenders, and proceeds of maturing financial assets
- The Government has access to financing facilities, of which the total unused amount at 30 June 2017 was NZ\$959 million

NZDMO Foreign Currency ALM

- Assets and liabilities are valued daily on a mark-to-market basis
- Profit (or loss) is generated from changes in the market value of the portfolio
- Tactical trading is employed to increase profit or reduce risk
- Comprehensive risk measures and limits are used (VaR, stop loss limits, stress testing)
- Risk adjusted performance measurement has been developed to assess profits against risk utilisation

Integrated ALM Approach



Manage both portfolios together as asset and liability or net liability portfolio and undertake hedging of risks and netting of payment flows

- use financial assets (including derivatives) to actively manage currency, interest rate and liquidity risk
- seek to minimise the “cost of carry”
- primarily hedge the cash flows for current budget year

Practical Example

Debt Service Payments

- For debt payments due over the next 1, 3, 6 & 12 months:
 - identify each principal and interest payment by currency, amount and due date
 - each week, hedge the position and maintain on rolling 3-month basis

Financial Asset Portfolios

- Allocate an equivalent amount:
 - match each cash flow by currency, amount and due date
 - invest to match cash flows or cover forward using derivatives
 - monitor net position and unmatched exposures

